

Arizona Department of Insurance

2006 Market Monitoring

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Homeowners' Insurance

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I. Rate System:

Arizona's "open competition" law, applicable to Homeowners' (HOs) insurance, prohibits insurers from charging excessive, inadequate or unfairly discriminatory rates or rates that will have the effect of destroying competition or establishing a monopoly. As a matter of law, the Department cannot find a rate to be excessive if "a reasonable degree of price competition" ("RDPC") exists at the consumer level. The law presumes a competitive market exists unless the Director, after a public hearing, determines that a RDPC does not exist in the market.

II. Market Monitoring Methodology:

The Department relies upon insurers' rate filings and their annual statements filed with the Department, insurers' responses to an annual Department survey, current trade press articles, and A.M. Best data to monitor the market.

The purpose of market monitoring is twofold: to assist the Director in determining whether competition exists; and, assist consumers with their questions and concerns about the availability of insurance.

III. Annual Statement Data:

The 2005 annual statements for all HO segments evidence that:

- The incurred loss ratio increased slightly (36.24%, 2005) from the prior year (33.79%, 2004).
- Direct written premium ("DWP") increased 6.91% (\$1,093,484,529 in 2005 compared to \$1,017,914,297 in 2004).
- Fifteen groups wrote 1% or more of the market. Within those groups, only 18 insurers wrote at least 1% of the market, an increase over the 2004 total of 17. Of these 18 insurers, the insurer with the smallest market share wrote more than \$11 million in DWP.
- Only 101 insurers wrote \$100,000 or more in premium (the same number in 2004).
- More insurers entered (9) than exited (6) and most exits were due to consolidations and acquisitions rather than to insurers simply withdrawing from the market of their own accord.
- The Top 5 insurers wrote \$25,149,196 more in DWP than in 2004 for an increase of 4.2%.
- The combined market share of the Top 25 insurers decreased by 2.24% in 2005 compared to 2004.

Historical Experience (All Insurers Page 20, Line 04, Annual Statement Data, Year Ending December 31)

	1	2	3
CY	Written Premium	Earned	Paid Losses
2005	\$1,093,484,529	\$1,051,411,684	\$390,860,273
2004	\$1,017,914,297	\$966,650,063	\$341,978,123
2003	\$911,327,662	\$850,351,436	\$420,650,238
2002	\$772,230,481	\$696,864,381	\$487,672,489
	4	5	
CY	Incurred Losses	Incurred Loss Ratio (Col 4/ Col 2)	
2005	\$380,987,524	36.24%	
2004	\$326,658,224	33.79%	
2003	\$441,190,481	51.88%	
2002	\$520,693,277	74.72%	

IV. Survey Responses:

In 2006, 129 insurers responded to the Department's HOs' survey of which 95 with a 2005 market share of 90.71% completed the survey.

Most insurers completing surveys responded that:

- HOs are a major national line for those insurers.
- Coverage availability is substantially the same as in 2005.
- Competition for HOs business is high or intense in Arizona.
- HOs business is important to their presence and success in Arizona.
- It is easy to enter the Arizona HOs market.
- Arizona's Open Competition law is highly effective.
- Reinsurance is not a problem.
- The most current Hard Market Stage of the Underwriting Cycle negatively impacted them and influenced their decisions in HOs.
- The market shows more signs of softening. Fifteen percent of the market reported that prices have substantially decreased.
- The national market in some manner and to some degree impacts insurer's local HOs decisions in Arizona.
- They are actively seeking new business with more fervor (75 insurers up from 59 in 2005).
- The number of declinations and/or non-renewals has not substantially changed since 2005. Most insurers (86 up from 85 in 2005) will maintain their current underwriting approach, and five said they would begin to relax their underwriting restrictions by year-end 2006.

V. Major HOs Market Trends:

Trend # 1: Groups writing in Arizona continue to add eligible insurers but few increase their market share. Twelve additional companies from nine different groups reported new activity on their 2005 annual statements. Eight groups, each with an insurer in the Top 25,

control 49.24% of the market. The only group with any significant increase in market share was the Allstate Group (2.76% increase) due to the addition of the Encompass companies (formerly CNA group).

Trend # 2: The market is concentrated in a few insurers among which competition is intense. The Top 5 continue to have a sizable portion of the market (55.37%, 2005; 57.04%, 2004) and competition is intense. Four of the Top 5 lost market share in 2005.

Rank	Company	2005 Market Share
1.	State Farm Fire & Cas Co	19.81%
2.	Farmers IC Of AZ	13.77%
3.	American Family Mutual IC	9.88%
4.	Allstate IC	7.62%
5.	Allstate P&C IC	4.29%
	Total:	55.37%

Trend # 3: Fewer insurers report low historical underwriting profitability for the HOs line. Sixteen insurers having 35.59% (down from 20 insurers with 42.44% of the market in 2005) of the market responded that their underwriting profitability in this line was historically low.

Only fourteen insurers with a combined market share of 5.56% (nine in 2005) out of 95 insurers reported that they had made any meaningful underwriting profit on their Arizona HOs writings.

Trend # 4: Not all insurers with authority to write HO insurance are actually writing HO insurance. While 203 insurers reported some HOs activity in their 2005 annual statements, only 75 said they are seeking new business (59 said they were seeking new business in 2005). The remaining insurers have the legal authority to write HOs in Arizona, but have elected not to actively participate in the market for reasons

of their own. Nonetheless, these latent insurers, although currently not actively seeking new business, can immediately enter the market at any time if they wish.

Trend # 5: Insurers view the level of competition in the market as high. Fifty-six of the responding insurers (50 in 2005) controlling 78.65% of the market said that, in their opinion, the level of competition in the HO market was high.

Trend # 6: Insurers intend to maintain their current underwriting stance through year-end 2006. This is the third consecutive year that almost all (86 out of 95) responding insurers reported they were maintaining their current underwriting stance and not moving toward a more conservative one. As a result, consumers will enjoy the benefits of a stable market.

Trend # 7: The incurred loss ratio increased over 2004. The Arizona 2005 all-company incurred loss ratio increased to 36.24%, up from 29.23% in 2004. Traditionally, there are peaks and valleys in HO loss ratios, primarily due to the volatility of storm and wildfire property claims. Even with the 2005 wildfires, the HO line remains profitable.

Trend # 8: Mold litigation claims against Arizona HO insurers continue, but the number of suits have declined dramatically. The number of insurers that experienced a mold claim within the past three years decreased from 37 in 2005 to 25 in 2006.

Trend # 9: The market is showing signs of softening. In 2005, the Market Share Weighted Average Total Rate Change was - 5.84% (-1.11% in 2004). Dry weather conditions, storm and wildfire exposures will impact the possibility of continued market softening in 2006.

Trend # 10: More insurers entered the market than exited. Nine insurers entered the market and six exited. The insurers that entered wrote \$14,517,351 in DWP during 2005 (1.33% market share).

VI. Conclusions:

Overall, the Arizona HO market has improved. Coverage is readily available and at competitive prices; competition is healthy; consumers have a choice among insurers; insurers are maintaining their underwriting stance resulting in consistency and stability in the market; and the market is softening with more insurers taking rate decreases.